



1940

Economic Conditions Governmental Finance United States Securities

New York, April, 1940

General Business Conditions

THE month of March has been another quiet period in business and the markets. As a rule the opening of outdoor work and preparations for Spring activity bring a pickup around this time, but the seasonal influence has been a minor factor, as was to be expected after the high production during the Winter. So far as the basic industries are concerned the trend of operations has continued downward. In general, new orders have not equalled production, and as their backlogs run down they are curtailing accordingly.

Among the different industries, however, the situation varies considerably. As in January and February, the sharpest contraction has been in steel output. At the other extreme, war demands are keeping airplane and machine tool plants and shipyards at capacity and are inducing expansion. It is unusual to find business in a downward trend while producers in many heavy goods lines are sold ahead and some have more large orders in prospect. But war demands are concentrated, while industries depending chiefly upon the domestic market, and steel in particular, are compelled to retrace their steps after the Fall boom.

The textile industries are slow to curtail, although operations are down from the peak. Electrical equipment companies are busy with good backlogs of orders for heavy equipment, and their household appliance business has made a satisfactory seasonal gain. In other cases where the Spring rise is usually vigorous, sales and production have not shown as much improvement as usual. The automobile industry is in that position. However, mid-March reports were better than those earlier in the month. Failure of automobile sales to make the full seasonal rise should cause no great surprise or disappointment, in view of the exceptionally good six months the industry has had, which probably included some pushing ahead of Spring buying.

In terms of the composite indexes of industrial production, adjusted for seasonal variations, the drop in March has been substantially

less than in January and February. According to preliminary indications the Federal Reserve Board's index for the month may be about 105 (1923-25 average = 100). The peak in December was 128, January 119, February 109. From December the indicated drop is 18 per cent, of which approximately one-half represents actual curtailment of production, while the other half is an adjustment of the figures to allow for failure to make the normal seasonal gains. This decline has been among the sharpest ever known.

Hopes of an Upturn

With three months of severe contraction of business left behind, and the rate of decline slackening, hopes that the drop has about run its course are widely expressed; but however warranted these hopes may prove to be, there are as yet no plain signs of a turn. The causes of the curtailment, while complex, may be summed up as a discrepancy between new orders and production, and in many industries this discrepancy is still considerable. Although the steel operating rate has dropped to around 60 per cent of capacity compared with an average of nearly 70 in February, new orders have continued substantially below output. How long this can carry on, or at what point the balance will be restored, is largely guesswork. Most observers concede that steel production is now below consumption, and that orders must pick up unless buyers wish to cut heavily into stocks, but the degree to which inventories will be drawn down is the question.

The cotton mills have had spurts of improved business, but on the whole their sales have fallen considerably short of production, and price concessions have not stimulated general buying interest. Fall woolen goods have had a slow opening. Sporadic improvement in leather and paper has not turned into broad buying. Non-ferrous metal markets have been quiet during the month; this, however, was to be expected following the heavy sales in February.

Evidently buyers are still well supplied as result of their forward orders last Fall, and

have not been disposed to move ahead again. Those who expect early improvement are doing little in anticipation. On the other hand, there is plainly no pressure for liquidation. Current comment indicates that sentiment is prepared for absence of a marked upturn in the near future, and that any adjustments still necessary in productive activity will be received with patience. The sideways trend of the markets indicates a waiting attitude, rather than one of either optimism or pessimism.

Factors in the Outlook

Until the recession reaches a definite stopping place, fears that it will feed upon itself and spiral downward, with consumption contracting and buying reduced to a hand-to-mouth basis, will doubtless demand consideration. The pessimistic argument is that inventories are large and that the new capital expenditures needed to maintain activity as present orders run out are not in sight. There is no disagreement as to the fact that inventories have increased, although most figures indicate that they have not climbed as high as the peak in 1937. Probably, however, the inventories are not the most important element in the situation. If they prove to be troublesome it will be not because of their size, but because the flow of trade is somewhere impeded, new investment blocked, and business confidence upset again. The real question is what the policy will be toward maintaining inventories and commitments, and the attitude will be influenced by war and political developments, as well as by the state of trade.

Probably the concentration of capital goods orders which occurred last Fall included business which was originally intended for 1940, and thus leaves fewer new orders to be placed this Spring. A major offset, however, is the increase in export trade. For the third successive month, merchandise exports in February were encouraging. They totaled \$347,000,000, an increase of 59 per cent over a year ago; and compared with the December-January level of \$368,000,000 each, the drop reflected only a shorter month. The continued high rate of shipments of metals and metal products, machinery, aircraft and chemicals is the encouraging element, since the future promise lies mainly in these groups, and the outlook for agricultural exports is not bright. At the rate of the past three months, exports for the year would total nearly \$4,500,000,000, an increase of almost \$1,300,000,000 over 1939.

It is fair to say that the best hope of sustained capital expenditures is to be found in sustained trade, export or domestic. If trade holds up investment will be induced, prices supported, and good sized inventories carried. One of the strong points in the trade outlook is the fact that prices, living costs and industrial costs have not been raised dangerously, or the rela-

tions between them greatly disturbed. Productivity is high; and price relationships between farm and industrial products on the whole are better than before the war.

A "Peace Scare"

The European news has caused some uncertainties, in a situation where business is counting upon war demand as a bullish factor. Although peace would be the greatest blessing that the world could possibly receive, the reports of peace moves during the past month have been commonly described as a "peace scare", and have been a cause of hesitation in the markets. There may be other "peace scares", and they emphasize the fact that the war is a wholly abnormal, unstable and unpredictable element in the business situation. If it should end, demands on some industries would be lighter, at least temporarily, and buyers would probably be inclined to let inventories run down more than otherwise. On the other hand, most observers agree that a long and in due course a more active war is more likely than a peace within any foreseeable time, and that it is reasonable to expect a very considerable volume of orders from the belligerents.

In any case business in this country is far short of being on a war basis, and is guarding against policies that would leave the situation vulnerable. Only a few industries have been asked to expand for war purposes, and all are making sure that new plant and equipment can be paid for rapidly and either charged off without loss or operated profitably in peace-time. Business men not directly affected by the war have altered, since last September, their ideas as to its stimulus to prices and industrial activity. The degree in which the boom has already been corrected has naturally strengthened the situation.

Money and Banking

Gold imports into the United States during the first three weeks of March aggregated \$200,000,000 compared with \$197,000,000 in the full month of February. Apart from metal placed under earmark, the month's imports of gold have added to the excess reserves of the banks, carrying the total for the member institutions of the Federal Reserve System to a new peak at \$5,780,000,000 on the 13th. During the ensuing week income tax collections cut the total sharply, but by the end of the month the total was again rising, with every prospect of reaching new high levels under the influence of continued gold imports and Treasury disbursements of accumulated tax money.

United States Government bonds were strong, influenced by peace talk early in the month and by the Treasury's March financing program omitting a cash offering and consisting only of the refunding of the June 1½ per

cent notes with new five-year $\frac{3}{4}$ per cent notes instead of with an issue of longer maturity, as had been generally expected. On an average the longer Treasury bonds rose over a point to new high levels for 1940.

The volume of new corporate and municipal issues fell off considerably in March, thus giving the market an opportunity to absorb the heavier supply of offerings of the previous month. As a result distribution of several issues which had proved somewhat slow was completed, and at the close of the month there was no important volume of undigested issues remaining in the market.

The Decline in "Free" Sterling

The free market rate for the pound sterling has declined sharply during the past month, following issuance of new regulations by the British authorities governing payment for British exports. The drop has caused concern to some exporters of this country, and to industries which have to compete with British products, although its consequences here are limited by the fact that only a part of the sterling market is affected. The situation is not to be judged by the experience of 1931 and 1932, when the depreciation of the pound was depressing dollar prices continuously. Compared with those years, there are more differences now than similarities; in fact, there has never been a like situation in sterling exchange.

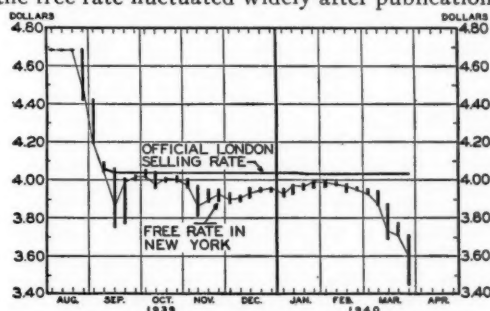
The new regulations, issued March 8 and effective March 25, provide that exports of certain major commodities from Great Britain, India, Burma and the Colonies to specified countries must be paid for either in specified currencies (dollars, belgas, Swiss francs and Dutch and Netherlands East Indian guilders) or in sterling purchased at the official rate of exchange. The commodities affected are rubber, tin and tin ore, jute and jute products, whiskey and furs. Australia has established a similar regulation covering her exports, of which the most important for the United States is wool.

This means that some of our chief imports from the British Empire (if contracted for since March 9) must be paid for on the basis of the official sterling rate of $\$4.03\frac{1}{2}$. Importers of these commodities are therefore eliminated as buyers of free sterling. This is the chief reason for the drop in the free rate. For the same reason, the free rate hereafter will not influence the dollar prices of these commodities, and its depreciation exerts no depressing effect upon them.

On the other hand, many other important commodities such as West African cocoa, Indian tea and shellac, and particularly all imports of British manufactured goods, may still be paid for in free sterling. In these cases, other things being equal, the sterling decline tends to reduce the price of these products in

this and other competitive markets. American exporters of manufactured goods may find British competition stronger, and sale of British merchandise in this country may be facilitated. Nevertheless it would be a mistake to jump to conclusions. Experience has shown that a depreciated currency is never more than a temporary advantage to export trade; and at present the sterling quotation is not the only element in the ability of Great Britain to export, or even the most important one. The sterling depreciation since the outbreak of the war has been offset to a very substantial degree by the rise of prices in Great Britain, which tends to maintain the prices of British products expressed in other currencies, despite the lower pound. Shipping difficulties and higher freight rates are to be considered. Moreover, Great Britain is at war and must use her factories and labor to prosecute the war. All the evidence shows that she is making a desperate effort to produce greater quantities of goods for export, but whether she can succeed, while fighting a war, remains to be demonstrated.

As will be seen from the accompanying chart, the free rate fluctuated widely after publication



Pound Sterling Rates in New York
(Weekly high, low and closing; latest closing as of March 28)

of the regulation, dropping to $\$3.45\frac{1}{4}$, the lowest quotation for the pound since April 1933. This was about 60 cents (or 15 per cent) below the official rate of $\$4.03\frac{1}{2}$. In sympathy, all other "sterling area" currencies established new lows, the French franc declining to 1.96 cents. For the purposes of currency regulation, the "sterling area" has been defined as including all of the British Empire (except Canada, Newfoundland and Hong Kong), all British Mandates and Protectorates, Egypt, Sudan and Iraq. It also includes the entire French Empire, by virtue of the stabilization of the franc at the rate of 176 $\frac{1}{2}$ francs to the pound, agreed upon last December.

The newly established free market rate for the Canadian dollar—another development of last month—moved sympathetically, dropping to a discount of 19 per cent, while the official control in Ottawa maintained its rate for United States dollars at 10 per cent premium for buying and 11 per cent for selling.

Sources of Sterling in the Free Market

The free market for sterling developed at the outbreak of the war in various neutral centers, of which New York has been the most important. The sterling offered at below the official rate has originated from a wide variety of transactions. The supply was supposedly much larger in the early days of the war, the flow from some of the important sources having diminished since then as a result of the tightening of exchange control. At present the most important sources of free sterling are (1) the payments for British imports from various countries (and French imports payable in sterling) for which the control does not provide foreign exchange at the official rate, (2) transfers abroad of interest and dividends on foreign capital invested in the "sterling area," and of proceeds from the sale of sterling securities by non-residents, and (3) settlement of claims on insurance policies held in British companies by non-residents.

Although most sterling transactions in New York have been at the free rate, as long as all importers could use free sterling, the London Economist estimated recently that the free markets have transacted since the beginning of the war, except at certain times, only between 5 and 10 per cent of the total exchange business in sterling—private and official. The bulk of British payments to other countries has been made at the official rate, which has been supported by gold shipments. Because of the new restrictions on the use of free exchange, the free market will become even narrower. Hence the decline is not to be construed as evidence that Great Britain's unfavorable balance of payments has exhausted the resources available for the support of the pound, but rather that these resources are being more effectively utilized.

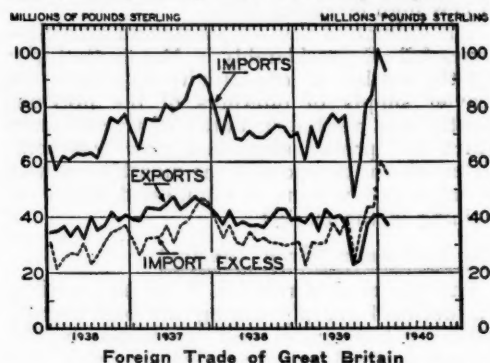
As a result of the extension of exchange control, the authorities will receive a larger share of the proceeds of Empire exports in foreign currencies, and at better rates. At the same time the transfer of funds from the Empire and the imports of non-essential goods will be discouraged because of the heavy depreciation of sterling in the free market. It should be recognized that the decline in free sterling itself tends to dry up the supply.

British Foreign Trade in January and February

Together with the partial mobilization of dollar securities in February, the new exchange regulations suggest that the British authorities are striving to assure themselves of a steady supply of foreign currencies to finance purchases of war materials abroad.

British merchandise imports rose considerably in the first two months of 1940, averaging nearly £100,000,000 monthly for the first time in almost ten years. Although exports have recovered to the pre-September level, they

have failed to keep pace with imports, despite the depreciation of the sterling. As a consequence, as will be seen from the accompanying chart, the January and February import ex-



cess aggregated about £116,000,000, or £62,000,000 more than in the same months a year ago. Such a record would mean almost doubling last year's trade deficit, without compensating increase in invisible credits which normally pay for it. On the contrary, such invisible credits as income from investments and earnings from shipping and commissions have been reduced as a result of hostilities.

However, a substantial part of the increased expenditures for merchandise imports probably is being spent within the sterling area. Indications of this trend are found in the rising industrial output and exports of the Dominions, India and other parts of the British Empire, and in the growing accumulation of sterling balances in the Empire Central Banks. Sterling securities held by the Reserve Bank of India, for example, and the sterling balances of the Reserve Bank of New Zealand have more than doubled in the first five months of the war, while the London balances of the Commonwealth Bank of Australia rose in the same period by about £13,000,000 to £45,000,000.

Nevertheless, the demand for dollars also has risen substantially, in view of the heavy machine tool, armament and aircraft buying here by the British and French Purchasing Commissions. From £45,000,000 in November, when the Neutrality Act was revised, our exports to the two Allied Powers rose to \$106,000,000 in January, while our imports from them were only \$22,000,000.

Profits of Leading Corporations, 1938-39

The marked improvement of earnings in most lines of business last year, which accompanied the sharp increase in industrial production and trade and was indicated by early reports, is confirmed by the annual reports now issued by a majority of the leading corporations. A tabulation of the published statements of 2,480 companies representing all major lines

shows combined net profits, after taxes and less deficits, of approximately \$3,456,000,000. This compares with a total of \$2,119,000,000 for the same companies in 1938, when earnings in most lines were relatively low and large numbers of companies operated at a deficit.

Capital, surplus and undivided profits of this group aggregated more than \$55,500,000,000 at the beginning of 1939, upon which the year's profits were at an average rate of 6.2 per cent. as against a rate of only 3.8 per cent in 1938. Following is a condensed summary of the gains by major divisions:

Summary of Net Profits of Leading Corporations in 1938 and 1939

(In Millions of Dollars)

No.	Division	Net Profits 1938	Net Profits 1939	% Change 1938-39	% Return 1938	% Return 1939
1,440	Manufacturing	\$1,068	\$1,938	+81	4.6	8.5
131	Mining & quar.	118*	169*	+43	4.2	6.3
229	Transportation	D-124	102	+....	....	0.8
124	Public utilities	518	599	+16	5.8	6.9
149	Trade	155	206	+33	8.6	11.3
84	Service & constr.	40	44	+10	5.9	6.3
323	Finance	346	398	+15	7.0	7.9
2,480	Total	\$2,119	\$3,456	+63	3.8	6.2

D-Deficit. * Before certain charges.

Despite the upturn in profits last year, the level of earnings was still somewhat below that of 1937—the peak of the recovery period—when our tabulation of a similar group of leading companies showed a return of 7.2 per cent. In the year 1929, the rate was 10.6 per cent.

The more detailed summary, classified by some sixty major industrial groups, gives a fairly broad sampling and shows the highly uneven character of the recovery last year. As pointed out heretofore, the earnings reported in the published statements of the larger corporations are useful as showing trends, but tend to run above the average rates for business as a whole, which become available later in the official "Statistics of Income".

Moreover, in some instances even the published statements of leading companies, taking the record of good years with the poor over a period of time, tend to overstate the average rate of real earnings. This is due to the fact that special adjustments, made from time to time in connection with writing down valuations of plant and equipment, or with setting up reserves against investments and intangible assets, are often charged directly against capital or surplus and not reflected in the profit-and-loss account. In reports for the year 1939, numerous special charges of this kind were made for writing down the dollar value of foreign exchange, foreign branches and foreign subsidiaries.

Manufacturing, Mining and Trade

In the manufacturing industries, which comprise the largest main division of our tabulation, the results shown by the 1,440 companies are similar to those given for 960 companies

last month, but the totals now include many more of the large organizations in the food, beverage, chemical, petroleum refining and other fields.

In the mining industries, the nonferrous metal producers benefitted last year by a marked increase in demand and by better prices. Coal mining companies increased their sales, and reduced the combined net deficit of the group reporting. Most oil and gas producers reported lower earnings last year, due to restrictions upon output and lower prices received for crude petroleum.

Sales figures, now being reported to shareholders by an increasing number of manufacturing companies, show wide variations in the gains made last year. In the capital goods lines, such as steel, machinery and other heavy materials and equipment, which experienced sharp declines between 1937 and 1938, there were increases in sales volume last year ranging from 25 to over 100 per cent for representative companies. In the consumers' goods lines, where the curtailment in 1938 had been less severe, the increases in 1939 ranged from 5 to 25 per cent. There were, of course, numerous excep-

Net Profit on Sales of Leading Corporations in 1938 and 1939

(In Thousands of Dollars)

No.	Manufacturing	Sales 1939	Profits* 1939	% Profits to Sales 1939	% Profits to Sales 1938
15	Baking	\$ 397,034	\$ 24,657	6.2	6.5
11	Dairy products	756,189	28,432	3.8	8.1
18	Meat packing	2,288,594	27,297	1.2	D-0.3
27	Sugar	279,405	12,752	4.6	0.6
83	Food products—misc.	585,067	48,732	8.3	7.8
32	Beverages	255,282	21,790	8.5	9.4
15	Tobacco products	965,106	87,617	9.1	9.0
24	Cotton goods	261,196	7,342	2.8	D-2.9
43	Textile products—other	411,698	20,629	5.0	D-1.5
15	Shoes	261,559	12,333	4.7	2.9
19	Rubber products	805,345	42,700	5.3	3.6
35	Paper products	379,883	23,848	6.3	1.9
28	Chemicals	407,516	34,694	8.5	6.7
18	Drugs, soap, etc.	621,830	61,539	9.9	9.4
23	Petroleum products	1,396,770	103,495	7.4	5.6
25	Stone, clay and glass	417,394	41,801	10.0	6.0
93	Iron and steel	2,508,809	132,856	5.3	D-0.6
9	Agricultural implements	439,150	26,996	6.1	6.1
21	Building equipment	311,634	13,412	5.9	1.4
26	Electrical equipment	968,893	90,656	9.4	6.3
26	Household equipment	175,992	13,600	7.7	8.9
48	Machinery	330,049	22,358	6.8	4.1
12	Office equipment	238,906	20,611	8.6	8.8
14	Railway equipment	172,350	8,204	4.8	D-4.3
18	Aircraft and parts	238,600	26,854	11.3	8.5
40	Metal products—other	634,039	50,622	8.0	5.1
19	Automobiles	2,330,783	225,785	9.7	6.0
20	Auto equipment	257,728	14,801	5.7	D-0.7
83	Misc. manufacturing	769,893	49,271	6.4	4.5
760	Total manufacturing	\$19,856,699	\$1,300,244	6.5	4.0
Trade					
17	Chains—food	991,523	17,168	1.7	1.1
42	Chains—other	1,647,476	93,936	5.7	5.1
25	Department stores	434,534	13,189	3.0	2.0
5	Mail order	1,174,372	65,772	5.6	4.5
21	Misc. and wholesale	427,089	9,350	2.2	2.0
110	Total trade	\$ 4,675,494	\$ 199,415	4.3	3.5
870	Total mfg. and trade	\$24,532,193	\$1,499,659	6.1	3.9

D-Deficit. * Including investment and miscellaneous income.

PROFITS OF LEADING CORPORATIONS FOR THE YEARS 1938 AND 1939

Net Profits Are as Reported, After Depreciation, Interest, Taxes, and Other Charges and Reserves, but Before Dividends.—Net Worth Includes Book Value of Outstanding Preferred and Common Stock and Surplus Account at Beginning of Each Year.
(In Thousands of Dollars)

No.	Industrial Groups	Net Profits Years		Per Cent Change†	Net Worth January 1		Per Cent Return	
		1938	1939		1938	1939	1938	1939
22	Baking	\$ 27,168	\$ 27,312	+ 0.5	\$ 315,778	\$ 314,498	8.6	8.7
17	Dairy products	23,928	28,905	+20.8	284,632	291,368	8.4	9.9
20	Meat packing	D-5,980	27,370	+	565,363	557,144	.....	4.9
86	Sugar	7,332	17,986	+	460,940	440,768	1.6	4.1
72	Misc. food products	87,261	99,530	+14.1	944,685	962,664	9.2	10.3
167	Total food products	139,709	201,103	+43.9	2,571,398	2,566,437	5.4	7.8
20	Soft drinks	34,217	39,140	+14.4	97,209	104,383	35.2	37.5
32	Brewing	12,274	15,655	+27.5	81,395	89,310	15.1	17.5
13	Distilling	11,760	11,171	- 5.0	99,049	112,015	11.9	10.0
65	Total beverages	58,251	65,966	+13.2	277,653	305,708	21.0	21.6
23	Tobacco products	93,085	96,385	+ 3.5	726,065	733,661	12.3	13.1
44	Cotton goods	D-7,582	9,844	+	287,369	270,128	.....	3.6
14	Silk and rayon	3,990	13,405	+	116,294	116,421	3.4	11.5
8	Woolen goods	D-6,332	4,066	+	102,160	95,227	.....	4.3
25	Knitted goods	3,475	5,366	+54.4	66,533	68,173	5.2	7.9
41	Misc. textile products	D-1,783	22,741	+	254,374	256,947	.....	8.9
132	Total textile products	D-8,232	55,422	+	826,730	806,896	.....	6.9
28	Clothing and apparel	2,944	11,426	+	111,983	109,371	2.6	10.4
8	Leather tanning	D-4,754	3,430	+	50,110	44,496	.....	7.7
20	Shoes, etc.	7,421	12,235	+64.9	178,589	177,500	4.2	6.9
28	Total leather products	2,667	15,665	+	228,699	221,996	1.2	7.1
26	Rubber products	23,869	44,410	+86.1	472,936	472,730	5.0	9.4
40	Wood products	2,688	11,422	+	160,488	162,623	1.7	7.0
73	Paper products	21,990	41,434	+88.4	644,182	645,839	3.4	6.4
34	Printing and publishing	7,437	13,274	+78.5	188,593	185,315	3.9	7.2
44	Chemicals, industrial, etc.	120,982	205,458	+69.8	1,551,000	1,592,167	7.8	12.9
27	Drugs, soap, etc.	56,195	75,987	+35.2	404,261	388,352	13.9	19.6
8	Fertilizer	2,782	1,777	-36.1	80,744	81,561	3.4	2.2
14	Paint and varnish	7,312	17,340	+	212,550	213,102	3.4	8.1
93	Total chemical products	187,271	300,562	+60.5	2,248,555	2,275,182	8.3	13.2
39	Petroleum products	190,045	222,493	+17.1	4,119,707	4,126,218	4.6	5.4
27	Cement, gypsum, etc.	10,647	19,283	+81.1	265,004	257,992	4.0	7.5
33	Other stone, clay & glass.....	27,244	50,381	+84.9	505,382	500,422	5.4	10.1
60	Total stone, clay & glass.....	37,891	69,664	+83.9	770,386	758,414	4.9	9.2
53	Iron and steel	D-8,388	142,215	+	3,506,523	3,191,521	.....	4.5
13	Agricultural implements	36,217	28,412	-21.6	546,035	553,667	6.6	5.1
44	Building equipment	2,343	25,273	+	400,669	383,720	0.6	6.6
61	Electrical equipment	55,284	101,261	+83.2	962,479	968,706	5.7	10.5
53	Hardware and tools	13,936	34,413	+	312,347	310,288	4.5	11.1
40	Household equipment	8,708	17,854	+	153,465	152,369	5.7	11.7
114	Machinery	35,791	50,119	+40.0	533,352	532,810	6.1	8.6
19	Office equipment	22,637	23,809	+ 5.2	225,504	228,783	10.0	10.4
29	Railway equipment	D-5,760	15,383	+	728,376	705,746	.....	21.8
25	Aircraft and parts	14,281	27,527	+92.8	122,011	131,126	11.7	21.0
69	Misc. metal products	27,916	58,297	+	589,111	587,172	4.7	9.9
525	Total metal products	202,965	524,563	+	8,129,875	7,796,908	2.5	6.7
26	Automobiles—complete	101,430	224,468	+	1,389,011	1,412,814	7.3	15.9
54	Auto equipment	D- 444	30,675	+	245,503	239,429	.....	12.8
80	Total automobiles	101,036	255,143	+	1,634,514	1,652,243	6.2	15.4
27	Misc. manufacturing	3,895	8,875	+	97,524	96,607	4.0	9.2
1,440	Total manufacturing	1,067,511	1,937,807	+81.5	23,209,788	22,916,148	4.6	8.5
27	Coal mining	D-5,908*	D-1,105*	.....	456,842	430,764	.....	.....
52	Metal mining	94,289*	144,187*	+52.9	1,913,068	1,862,905	4.9	7.7
41	Oil and gas	19,907*	13,266*	-33.4	317,601	275,636	6.3	4.8
11	Misc. mining, quarrying	9,365*	12,154*	+29.8	111,322	108,719	8.4	11.2
131	Total mining, quarrying	117,653*	168,502*	+43.2	2,798,833	2,678,024	4.2	6.3
138	Class I railroads	D-121,349	94,639	+	13,248,547	12,805,636	.....	0.7
30	Traction and bus	D- 11,231	D-9,977	.....	500,680	489,032	.....	.....
13	Shipping	1,976	5,211	+	121,906	121,603	1.6	4.3
48	Misc. transportation (a).....	6,526	12,564	+92.5	230,561	230,210	2.8	5.5
229	Total transportation	D-124,078	102,437	+	14,101,674	13,646,481	.....	0.8
95	Electricity, gas, etc. (b).....	353,091	396,281	+12.2	6,037,168	5,878,690	5.8	6.7
29	Telephone and telegraph	164,697	203,162	+23.4	2,845,868	2,795,693	5.8	7.3
124	Total public utilities	517,788	599,443	+15.8	8,883,036	8,674,383	5.8	6.9
19	Chain stores—food	13,673	20,262	+48.2	192,780	194,848	7.1	10.4
48	Chain stores—other	79,422	95,038	+19.7	702,192	716,353	11.3	13.3
32	Department stores	8,909	13,100	+47.0	226,133	228,821	3.9	5.7
5	Mail order	44,346	65,772	+43.3	453,654	468,314	9.8	14.0
45	Misc. and wholesale	8,197	11,785	+43.8	214,142	215,960	2.8	5.5
149	Total trade	154,547	205,957	+33.3	1,788,901	1,824,796	8.6	11.3

PROFITS OF LEADING CORPORATIONS FOR THE YEARS 1938 AND 1939—Continued

No.	Industrial Groups	Net Profits Years		Per Cent Change†	Net Worth January 1		Per Cent Return	
		1938	1939		1938	1939	1938	1939
18	Amusements	27,696	26,033	— 6.0	415,465	427,038	6.7	6.1
21	Restaurant and hotel	D-1,624	28	+	79,466	77,640	.....	.....
24	Other business services	7,865	10,892	+38.5	103,445	104,208	7.6	10.5
21	Construction (c)	5,830	6,802	+16.7	80,275	80,405	7.3	8.5
84	Total service & construction..	39,767	43,755	+10.0	678,651	689,291	5.9	6.3
80	Commercial banks	164,548	191,071	+16.1	2,211,840	2,236,415	7.4	8.5
81	Insurance companies (d)	82,711	79,085	— 4.4	782,397	881,847	10.6	9.0
86	Investment companies (e).....	43,338	74,486	+71.7	1,375,377	1,373,005	3.2	5.4
34	Sales finance companies	55,366	54,599	— 2.3	441,584	449,797	12.7	12.1
42	Real estate companies	D- 640	D-813	.....	133,142	130,859	.....	.....
323	Total finance	345,873	398,428	+15.2	4,944,340	5,071,923	7.0	7.9
2,480	Grand total	\$2,119,061	\$3,456,339	+63.1	\$56,405,223	\$55,501,046	3.8	6.2

† Increases or decreases of more than 100 per cent not computed. D-Deficit. * Before certain charges. (a) Includes air transport, stockyards, docks, warehousing, pipe lines, etc. (b) Figures refer to shareholders only. Because of the large proportion of bonded indebtedness, actual return on the property investment is less than the above. (c) Includes shipbuilding. (d) Fire and casualty. Figures represent underwriting gain, and net interest, dividends and rents earned. (e) Net income shown as reported, not including such profits or losses on investments sold as were carried directly to surplus or reserve, nor changes in market value of portfolios.

tions in the case of individual companies, some of which, due to special circumstances, had declines in sales.

A group of 760 leading manufacturing companies reported aggregate net sales last year of approximately \$19,857,000,000, while their combined net profits (including investment and miscellaneous income) were \$1,300,000,000, or 6.5 per cent of sales. This compares with a rate of 4.0 per cent for a similar group in 1938, and 7.4 per cent in 1937. Net profits normally tend to increase, or decrease, much more sharply than changes in sales volume, due to the relative inflexibility of many operating and overhead costs. An additional factor in the improvement of profit margins in certain lines was the upward trend of commodity prices in 1939, following the stable or gradual downtrend of prices in 1938.

In the trade groups, an outstanding gain was made by the mail order companies, whose total sales (including branch retail stores) increased by 18 per cent. There were also sales increases by a majority of the food and other chains, department stores and wholesale houses. Combined sales of 110 leading trade corporations aggregated \$4,675,000,000 in 1939, while net profits were \$199,000,000, representing 4.3 per cent on sales. This compares with 3.5 per cent in 1938 and 3.6 per cent in 1937. These ratios of "net profit" should not be confused with the "gross profit" or spread between buying and selling prices, out of which must be paid wages and salaries, other operating expenses and taxes, before arriving at the "net profit" for the use and risk of the shareholders' capital invested in the business.

As indicated by the footnote to the table, the reported net profits of both manufacturing and trade companies include investment and miscellaneous income, such as interest, dividends, rents, royalties, income from service and repairs, etc., and consequently are higher than the net profit derived from sales alone.

Recovery in Railroad Earnings

Railroad traffic in 1939 exceeded the levels of 1938 throughout the year, but exceptionally large gains were made in the last four months, accompanying the expansion of general business activity. In September and October the sharpest upswing in freight traffic ever recorded was handled by the American railroads without appreciable delay or congestion. Although operating and maintenance expenses also increased, a substantial portion of the increased gross revenue was carried over into net operating income, which in the fourth quarter was the largest of any corresponding period since 1929.

For the year 1939 as a whole, total freight revenues of all class 1 steam railroads increased 14 per cent and passenger revenues 3 per cent. Total operating revenues increased 12 per cent and reached \$3,995,000,000, approximating those of the year 1937. There was net income, after operating expenses, taxes and interest charges, of almost \$95,000,000, which contrasts with a net deficit of \$121,000,000 in 1938 and was only moderately below the \$99,000,000 net income of 1937.

Public Utility Earnings and Taxes

A group of 95 leading systems supplying electric, gas and other services reported gross operating revenues of \$2,224,582,000, an increase of 5 per cent, due to the recovery in industrial demand and continued growth in residential consumption. Net income amounted to \$396,281,000, an increase of 12 per cent, and rate of return on net worth rose from 5.8 to 6.7 per cent. Average electric rates continued downward, despite the further rise in taxes which reached a new high level and averaged, for the industry as a whole, 16.2 per cent of gross revenues.

Part of the utility tax increase last year, however, was due to higher income taxes on increased net income. It is interesting to note

that the companies included in the tabulation were able to carry 39 per cent of their increase in gross revenues over into net income, showing the ability of operating companies in a period of expanding business to absorb increased taxes and other expenses.

American Telephone and Telegraph Company and its principal telephone subsidiaries had an increase of 5 per cent in operating revenues, and a gain of 21 per cent in net income. Taxes upon the Bell System rose to a new high of \$158,905,000 in 1939, compared with \$147,431,000 in 1938 and \$83,467,947 in 1929. Although operating revenues in 1939 exceeded those of the previous record year 1929 by 3 per cent, net income was 8 per cent lower while taxes were 90 per cent higher. Taxes represented an average charge of \$9.84 for every telephone in service last year, equal to 82 cents per month.

Financial Corporation Earnings

Operating earnings of a group of 80 leading commercial banks and trust companies were approximately the same as in the preceding year, but there was some increase in net profit, due to smaller losses on loans and investments. Fire and casualty insurance company earnings were around the same level as in 1938, with investment income showing some improvement but underwriting profit, affected by the reduction in automobile liability insurance rates, lower in some cases.

Most investment trusts showed an increase in reported net income last year, due to larger dividend income and to the non-recurrence of losses on securities sold, which some trusts charge against current income. Sales finance companies had a substantial increase in total volume of paper discounted but, because of lower interest rates, showed little change in net income.

Our "Mature Economy"

With the recession of business from the high levels of last Autumn, more is likely to be heard of the "mature economy" thesis. This thesis, born of the years of discouragement and disappointment since 1929, has gained considerable currency in the United States and has been influential in shaping public policies in recent years, in particular the policies regarding governmental expenditures. Our readers undoubtedly are familiar with the broad outlines of this thesis. Briefly stated, the central idea is that the United States is growing old and that progress is naturally slowing down. More specifically, it is pointed out that population growth is declining; that the United States has no more "frontiers"; that no new great industries are in sight. From this the argument proceeds that opportunities to invest capital are no longer sufficient to employ the available savings, and that with less employment for

capital there will be less employment for labor. Therefore, the government must assume a larger management of affairs and through its own enhanced spending and "investment" supply in part at least the stimulus heretofore provided by private enterprise.

Among economists most widely known for their support of the "maturity" view is Alvin H. Hansen, professor of economics at Harvard University. Speaking before the annual meeting of the American Economic Association in December, 1938, he said:

It is my growing conviction that the combined effect of the decline in population growth, together with the failure of any really important innovations of a magnitude sufficient to absorb large capital outlays weighs very heavily as an explanation for the failure of the recent recovery to reach full employment.

While Professor Hansen gives recognition to other factors, "particularly our failure to control the cost structure and to grapple effectively with specific situations, such as those presented by the railroads and by building construction," the emphasis clearly lies in the ideas expressed in the quotation given above.

Representative also of the same school of thought is the following from another paper* read before the same meeting:

Should new industries fail to materialize in sufficient volume to demand large private capital outlays, a continued expansion of the demand for capital goods appears to be contingent on the assumption of large responsibilities by local, state and federal governments to provide for the expansion of investment. Such expansion can take the form of large expenditures for public works projects and the development of capital facilities which tend to stimulate business enterprise, for instance, residential housing construction, roads, streets, sewage systems, airports, and rural electrification. These direct forms of expanding the demand for capital goods might well be combined with some means of changing the distribution of the national income so that large bodies of consumers may have enough purchasing power to require the physical expansion of existing industries.

Conclusions such as these, arrived at by serious students of economic trends, are evidently matters of concern. Business men are disturbed by them and are asking whether there is anything to be said by way of rejoinder. What reasons may be advanced for believing that these theories are based upon too pessimistic an estimate of American possibilities?

Periods of Pessimism Not New

In the first place, it is well to bear in mind that periods of distress and hard times always have been periods of doubt as to the future.

Probably the best known example of this was the classic lament of the first U. S. Commissioner of Labor, the Hon. Carroll D. Wright, appearing in his annual report for 1886, and reading in part as follows:

Industry has been enormously developed, cities have been transformed, distances covered, and a new set of economic tools has been given in profusion to rich countries, and in a more reasonable amount to poorer

*Effects of Current and Prospective Technological Developments Upon Capital Formation; David Weintraub, National Research Project, Works Progress Administration.

ones. What is strictly necessary has been done often times to superfluity. This full supply of economic tools to meet the wants of nearly all branches of commerce and industry is the most important factor in the present industrial depression. It is true that the discovery of new processes of manufacture will undoubtedly continue, but it will not leave room for marked extension, such as has been witnessed during the last fifty years, or afford remunerative employment of the vast amount of capital which has been created during that period. . . . The day of large profits is probably past. There may be room for further intensive, but not extensive, development of industry in the present area of civilization. . . . Supplying themselves with the full facilities for industry and commerce will give to each of the great nations of Europe and America something to do, but the part of each in this work will be small and far from enough to insure more than temporary activity.

Although Mr. Wright was an able economist, and well thought of in his day, his chief claim to fame now lies in the above utterance which proved so wrong—a fact that perhaps should serve as a warning to economists of our time.

Still another illustration may be cited, from Dr. Robert A. Millikan's book on *Evolution in Science and Religion*, in which the famous physicist, commenting upon a lecture which he heard in the early '90s, writes:

Then, summarizing this wonderfully complete, well verified, and apparently all inclusive set of laws and principles into which it seemed that all physical phenomena must forever fit, the speaker concluded that it was probable that all the great discoveries in physics had already been made and that future progress was to be looked for, not in bringing to light qualitatively new phenomena, but rather in making more exact quantitative measurements upon old phenomena.

Just a little more than one year later, and before I had ceased pondering over the aforementioned lecture, I was present in Berlin on Christmas Eve, 1895, when Prof. Roentgen presented to the German Physical Society his first X-ray photographs. . . .

As I listened and as the world listened, we all began to see that the nineteenth century physicists had taken themselves too seriously, that we had not come quite as near sounding the depths of the universe, even in the matter of fundamental physical principles, as we thought we had.

And there are other examples. The simple truth is that men's judgment is not to be relied upon in these matters. The birth of new industries is seldom, if ever, recognized at the time, and repeatedly men have prophesied that opportunities for growth and progress had come to an end, only to have their statements look foolish in the light of what came after. In each period, those holding these views have overlooked the fact that human wants are insatiable, that technological progress is constantly opening up new fields of development, and that increasingly greater capital investments are required.

True, the fact that it has been so in the past is not proof that it will always be so in the future. Each depression is in some respects unique, and in each new reasons are brought forward for doubting that the up-trend can be resumed. The present is no exception, and while the experience of the past may convey a large measure of assurance, it is clearly necessary to examine certain of the reasons given why "this time" the outcome may be different.

Effect of the Decline in Population Growth

First, as to the decline in population growth. It would be idle to deny this to be a matter of great significance; and yet there is no certainty that the country may not adjust itself to this change, as to former changes, or that the welfare of the people as a whole will suffer.

Even in the case of residential construction—usually thought of as particularly dependent upon population growth—pessimistic forecasts may easily prove to be premature. More important (from the standpoint of building) than the rate of increase of total population is the rate of increase in the number of families, which promises to decline much more slowly than the rate of increase in population itself. Thus we are told by W. C. Bober,* economist of the Johns-Manville Corporation, leading manufacturers of building materials, that "in spite of the fact that our population in 1949 will be growing at the rate of barely one-third the rate of the decade of the early 'twenties, nevertheless more people of home-owning age will be looking for homes in 1949 than in 1925, the year of our greatest building boom." The reason for this is that these people will have been born in the decades of the 'tens and 'twenties of this century when the birth rates were very much higher than they are today or than they will be in 1949.

And after that, is homebuilding likely to become a declining industry? Mr. Bober thinks not, for two reasons, (1) the vast possibilities that lie in the field of rehousing, and (2) the likelihood of continuing shifts of population, which tend to promote building activity. Both of these influences, he points out, have contributed to great building activity in Great Britain, although that country is much closer to a static population than we are. What fields for exploitation any substantial lowering of building costs would open up can only be guessed at, but certainly they would be large. There the barrier is not a stationary population, but obstacles such as high labor costs, high real estate taxes, and the difficulty of employing mass production technique.

For industries generally there may be even less reason for supposing that a slowing down of population growth necessarily means stagnation and under-employment. It has not turned out so in Great Britain, or in Sweden—also a country of declining population growth—or in France where population has been virtually stationary. One needs but look at China and India to realize that prosperity and well-being are not determined by size of population. What counts is the productivity of the people, which can be maintained, and even increased, whether the population is rising, declining or stationary.

*Address before the National Industrial Conference Board, Sept. 22, 1938.

Very probably a declining rate of population growth means that less of the national income will be spent on necessities (though there is still ample room for expansion there) and more on luxuries, thus bringing about a rise in the standard of living. From this some writers have concluded that the expansion of the future will be largely in the consumption goods industries, with opportunities for investment in capital goods diminishing. That the consumption goods industries should gain from a rising standard of living may be readily conceded, but that capital goods will not also participate is far from clear. One can hardly envision any considerable expansion in one without the other, for somehow the goods must be produced and distributed. In fact, with the constant technological improvement in industry and the tendency to use machinery and electric and steam power more and more to lighten human drudgery, one might perhaps be justified in concluding that potentialities for expansion in the heavy industries are greater now than ever before.

Disappearance of the "Frontier"

Second, there is the point about the lack of new "frontiers" beyond which to expand. It is true that most of the good land is now occupied and that our possibilities for further *extensive* development are limited; but the possibilities for further *intensive* development are only just beginning to be realized. It has been said aptly that there are no frontiers where human wants are concerned.

We have been hearing a great deal about the "one-third of the nation that is ill-fed, ill-clad and ill-housed," and figures on the distribution of incomes published by the National Resources Board have often been cited as evidence that we are still a long way from providing proper living conditions for a large section of our population. Such figures, and the conclusions usually drawn from them, certainly do not suggest that we have reached the saturation point in the satisfaction of wants, whatever may be said of frontiers in the geographical sense.

"No New Great Industries in Sight"

Third, there is the argument that there are no new great industries in sight. But are such developments ever "in sight" to contemporary eyes? Quotations given early in this article suggest not. The fact that we cannot foresee new developments comparable to the building of the railroads or the expansion of the automobile industry does not preclude the possibility of their taking place. Science and invention are working ceaselessly in the search for new products and better methods, and have the aid of tools and facilities far superior to those at the disposal of the early inventors. Commenting on the progress of invention, the

report of the Sub-committee on Technology to the National Resources Board said:

The large number of inventions made every year shows no tendency to diminish. On the contrary the trend is toward further increases. No cessation of social changes due to invention is to be expected. It is customary to speak of the present age as one of great change, as though it had been a turbulent transition period between two plateaus of calm, but such a conclusion is illusory. Though the rate of change may vary in the future there is no evidence whatever of a changeless peace ahead.

That the results of research will prove less productive of new opportunities for investments of capital and employment of labor in the future than in the past seems indeed difficult to believe. Nor is it necessary that any great new industry be discovered. As pointed out in a recent bulletin by the Machinery and Allied Products Institute of Chicago, "the more mature and elaborate a technology becomes, the more likely it is that expansion will occur through thousands of individually minor advances, rather than through a few inventions of a fundamental and revolutionary character." Of somewhat the same opinion is Professor W. I. King, of New York University, who, referring to the income figures of the National Resources Board, states that "as long as the modal family income in the United States is under \$1,000 per year, there certainly is no need to conjure up wants for new and unknown products or to establish new industries in order to find a market for far more goods than our present industries can produce." In the case of building, for example, one of the oldest of all industries, — what new industry could provide a stimulus greater than would come from a lowering of building costs, bringing decent housing within the buying power of the masses?

Opinions from Abroad

It is interesting to read what some foreign commentators are saying of the idea that the United States is "growing old".

Referring to assertions by American economists that the United States is now a "mature economy" which can hardly hope to increase its rate of production above the 1929 level, the Economist of London observes in its issue of December 2, 1939, that "it is difficult to take this theory seriously—or to know whether its partisans themselves take it seriously." Continuing, the Economist says:

If the United States, with its vast areas, its low debt, its inexhaustible natural resources, its rising population is a mature economy, what is Great Britain? And yet our "decadent" economy has contrived, during the decade when America was standing still, to go ahead as fast as on the average of the great Victorian era of expansion. Ten years ago the per capita National Income of the United States was one-third larger than the British; today it is probably no larger at all. The peculiar significance of this comparison lies in the fact that the British economy, before its recent spurt, seemed to be as completely becalmed as the American is now. In the 1920's it was Britain that stood still while other nations went ahead; in the 1930's America has taken the position we vacated. If Britain, inherently much the more "mature" of the two,

has found it possible, to regain a high rate of progress after a decade in the doldrums, there is no reason whatever to expect any different course of events in America.

***** The American economy seems to have forgotten, for the moment, how to grow. But the probable explanation of this economic anaemia is to be found not in any arrival at "maturity," but rather in the existence of institutional obstructions to a free flow of capital. *****

Writing in the October, 1939, Quarterly Review of the Skandinaviska Banken, Professor Gustav Cassel of the University of Stockholm, likewise takes issue with the pessimistic view of future economic progress. Referring to "much talk about profound structural changes" as impeding post-war progress, Professor Cassel says that earlier times likewise had "structural changes" and overcame them. He asks how far "irrational human actions" may be responsible for recent lack of progress, and says:

Progress has never been a machine. It has always been dependent on whether human forces working for increased progress have been allowed sufficient scope. It is possible to narrow that scope in such a degree that progress is stopped. But then people must not declare that the stagnation was necessary, or that it was idle to believe in the possibility of continued progress.

Where the Trouble Lies

The purpose of the foregoing discussion, as indicated at the outset, has been to review briefly the principal arguments against the "aging economy" doctrine. It is not within the province of this article—nor would there be space—to elaborate upon alternative explanations for the failure of the United States to achieve full recovery. Quotations from Professor Cassel and from the London Economist, cited above, suggest something as to the nature of the difficulties, and comments by other authorities are likewise instructive.

Thus, Professor King, in the article already quoted, says repeatedly, in varying language, that maladjustments in prices and wage relations (for which he blames employers, labor leaders and law makers about equally) have been the main cause of slow trade and unemployment since 1929. He sums up the "maturity" theory as follows:

The factors responsible for the present partial paralysis of industry in the United States are not related to the degree of maturity of our economic system but would affect any youthful economy just as adversely.

Unemployment is not the result of lack of capital, lack of industrial progress, or lack of new industries; as a matter of fact, the most backward, poverty-stricken countries have the least unemployment. Employment is a function of the price of labor. There is no indication that, with wage-rates conforming to the market demand, private industry cannot readily absorb the entire available labor supply or that there is any necessity whatever for expansion of government activities in order to create either full employment or opportunities for investment.

Dr. Leo Wolman, professor of economics at Columbia University, and well-known both as a student and as a man of practical experience in the labor field, has also emphasized the importance of labor policies in connection with unemployment. Speaking before the Academy of Political Science last Fall, he said:

In the United States since 1933—or perhaps since 1930—traditional labor policy has been completely overhauled. In the process influences of the market and the state of business have become subordinated to rules and regulations, embodied in laws, decisions of courts and boards, and the guiding principles of multifarious administrative agencies. * * * In so far as these rules and regulations have become effective, they have been reflected in the developments of wages and working conditions, the methods of labor relations, and of relief and social security. And it is in these areas that the clues to the relation of labor policy to unemployment must be sought.

Historically and logically improvement in wages and working conditions was associated with good business and increasing production. No one has ever supposed that they could be raised by mandate, in the absence of conditions capable of sustaining them at their higher levels. Our present labor policy is based on precisely that supposition.

In an article on "The Business Outlook" in the November, 1939, issue of the Atlantic Monthly, Dr. Sumner H. Slichter, professor of economics at Harvard University, takes the view that the greatest doubts over the capacity of industry to absorb the country's savings spring from uncertainties over the nature of public policy. "Will it," he asks, "be a help or a hindrance?" Continuing, he summarizes the problem before us in the following words:

The difference between the nineteenth century and the twentieth is not that sufficient expansion to absorb our savings was possible then and is impossible now. The difference consists in the nature of the obstacles to expansion.

In the nineteenth century, expansion depended upon the willingness of thousands of individuals to endure the hardships and dangers of life on the frontier. Today it depends upon the ability of millions of persons to see their common interest in the encouragement of investment, and their willingness to subordinate a multitude of special interests to the achievement of that supremely important general interest.

By policy, we can make ourselves rich or poor. By policy we can make it easy for the technicians to produce expansion and the opportunity and security which go with it (for the three are inseparable), or by policy we can shoulder ourselves with a crushing burden of chronic unemployment that will compel radical changes in our institutions and will threaten the existence of civil liberty itself.

We believe that this article might well close with the above quotation from Professor Slichter. Nevertheless, we wish, in conclusion, to make one more point suggested by this quotation and others preceding. The economic system has been subjected to terrific stresses and strains in recent years, first by the World War, and later, by the widespread social and economic readjustments since the depression. The changes from peace to war and back to peace, with their consequences, are not chargeable to the economic system. Obviously production, prices and trade were violently affected, and the efforts of governments to establish order added no little to the confusion. Apart from any question as to the merits or demerits of particular policies, it would seem evident that this period is totally unsuited as one by which to judge the dynamic qualities of private business enterprise. To reach conclusions and adopt long range policies on so inadequate a base might not only delay recovery, but lead to the consequences named in the quotation.

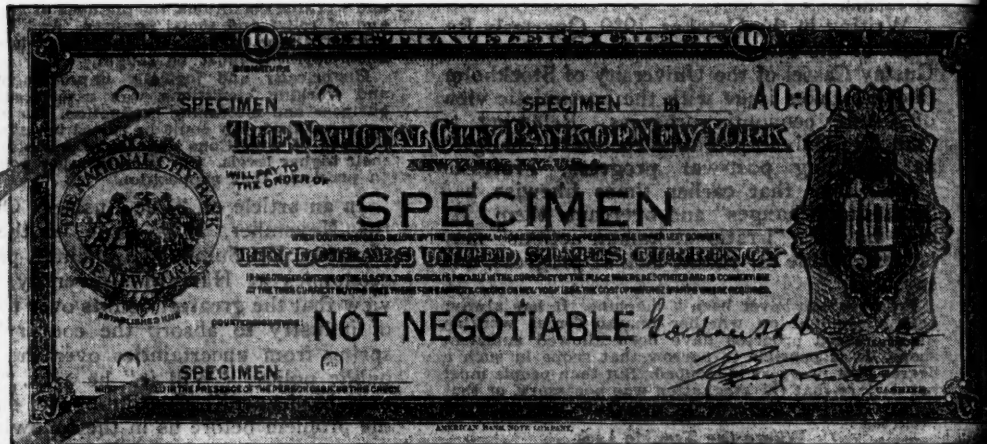
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